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ABSTRACT

The effectiveness of parent choice plans requires that schools-for-profit be given an equal opportunity to compete with government and nonprofit schools in the educational marketplace. Little information is available about schools-for-profit because most states do not gather separate statistical data on that category. However, the following characteristics can be derived from case studies that include evaluations of the Sylvan Learning Center, Huntington Learning Systems, and the Encyclopedia Britannica: (1) many elementary schools-for-profit offer day care programs as an add-on service; (2) policy decisions are made with regard to profitability; (3) the largest group of schools-for-profit serves the handicapped or disabled; (4) college counseling services are emerging in the for-profit sector as a result of parent dissatisfaction with high school counselors; and (5) out-of-school educational services, such as summer camps and music lessons, comprise a significant share of the for-profit market. The following advantages of schools-for-profit are discussed: (1) the producers have a direct personal stake in increasing productivity; (2) they are more responsive to parental inquiries, needs, and interests; (3) instructional services can be eliminated, modified, or added much more expeditiously than in public schools; (4) they are free from the restriction of state regulation and prescription intended to maximize teacher benefits; (5) they reduce the litigation costs of public education; (6) they provide an accurate guide to parental preferences; (7) they are responsive to changes in market conditions; and (8) they provide students with direct exposure to the principle of the generation of wealth. (FMW)

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PROFIT-SEEKING SCHOOLS

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My objective in this article is to invite attention to the importance of encouraging schools for profit. In the space available, it is impossible to convey the importance of this issue adequately; it may be helpful, however, to explain how I came to adopt my views concerning its importance.

In 1986, I published a book entitled Beyond Public Education. The main thesis of the book was that conventional school reform was, is, and would continue to be a futilitarian effort. By "conventional school reform" I refer to reforms that are not based upon basic changes in the governance structure of American education. Essentially, the contention is that the basic obstacles to improving education are its monopoly status and the fact that the services are overwhelmingly provided by government. Reforms that do not address these issues are unlikely to lead to significant improvement.

Beyond Public Education devoted a great deal of attention to the way various interest groups, primarily the public education lobby, were able to veto or sabotage desirable changes under our existing system of public education. In part, their veto power defines the problem; how do we change from a system in which producers have a stake in inefficiency to one in which they have a stake in higher levels of efficiency? With all of its limitations, the free enterprise system appears to be the most effective way to get interests working for instead of against a more efficient educational system.

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Nevertheless, the focus of Beyond Public Education was on demonstrating the inherent deficiencies of the existing system. The question of what to do about it was largely deferred to Privatization and Educational Choice. The latter is an effort to analyze the various modes of privatization from educational, economic, and political perspectives.

The modes of privatization include contracting out, vouchers, tuition tax credits, home schooling, and private learning centers. Each mode can be implemented in several different ways. As matters stand, however, these modes do not emphasize for profit enterprise. Home schooling is an example. Another is the fact that the overwhelming proportion of private schools are nonprofit organizations. One of the issues that concerned me was the claim that vouchers or tuition tax credits would bring the benefits of competition to education. Specifically, one of my concerns was whether we can or should expect the benefits of competition from nonprofit enterprise. This led me to review the literature on nonprofit organizations -- a literature that is growing rapidly due to the fact that our economy has been devoting a larger share of resources to the nonprofit sector in recent years. On the basis of this review, I reached two tentative conclusions:

1. There are strong reasons to doubt whether we can expect the benefits of competition in an industry dominated by nonprofit enterprise; and

2. To the extent that we can expect the benefits of competition from nonprofit enterprise, there may be reasons to question why such enterprise should be nonprofit. For example, in the hospital

field, nonprofits compete with for profit hospitals; an analysis of their operational similarities, including services provided the indigent, raises the question: What is or should be the justification for nonprofit status? Significantly, research on nonprofit organizations suggests that in some important respects, they are more like government bureaucracies than competitive for profit enterprise. This is especially true of managerial incentives, a much neglected issue in the educational reform movement.

Before elaborating on this point, let me comment briefly on our information about schools for profit. As far as I have been able to determine, very little information on the subject is available. The states typically classify schools as public or private; the latter are not categorized into for profit and nonprofit. Consequently, we lack reliable data on the number of schools for profit, their enrollments, costs, expenses, profits, programs, or educational effectiveness. Even the national organization of schools for profit lacks reliable information on these issues. In addition to the fact that most states do not collect separate data on schools for profit, difficult technical problems have yet to be resolved. For example, a school might offer two years of preschool and first grade. Comparisons to public schools would normally have to be based on comparable grade levels to be useful, but the data is not always available in this form. Obviously, allocations of income and expenses might be misleading if the grade levels are not comparable; likewise, educational comparisons are not likely to be useful if the grade levels are not comparable. As a matter of fact, the states do not define school in the same way. If "school" is defined as an enterprise that enrolls one or more grades required by state law, 96 to 99 percent of private schools are nonprofit.

Despite the lack of systematic data on schools for profit, anecedotal evidence about them is suggestive. Day care provides an illustration. In 1985, my interviews with operators of schools for profit in the San Francisco area revealed that most provided day care as an add-on, or were seriously considering it. Frequently, both parents worked and were not available to supervise their children between the close of school and parental arrival from employment. Many other children were from single parent families in which after-school care was essential to enable the parent to continue working. For the most part, the issues involved were normal business issues: How many parents would be willing to pay how much for various services? School management then had to decide its risks and costs and make a decision. The schools showed an interesting divergence on the issue of add-ons. Some offered a low basic rate with several options concerning additional services; others, reluctant to "nickel and dime" their parents frequently tended to fold in more services in the basic rate.

The point is that the decisions to offer day care were made in the same way as other business decisions. Significantly, at the time the schools for profit were providing day care for an additional fee, public schools were not doing so, even when many of their parents clearly would have paid for it.

The differences between the two situations were especially evident when I visited a school that required its students to wear uniforms. This school policy was a business decision. The owner of the school did not have to put the issue on the school board agenda, conduct interminable hearings, defend the policy against the objections of opponents, get bogged down in the color and design of the uniforms, and otherwise devote substantial resources to the policy or its implementation. If parents wanted to enroll their children, they had to accept the policy; if they didn't like it, they could enroll their children in a different school.

It requires little imagination to appreciate the differences between the decision-making process in this school for profit and a public school. In the latter, the issue could drag on for years; like sex education, it could be a never-ending source of community controversy over public school policy. If the decision is to be made in the economic system, the service provider does not have to satisfy everyone or even a majority of parents; it is only necessary to satisfy enough parents to achieve profitability. The superior responsiveness of the for profit sector in this situation is hardly debatable, yet it is all the more impressive in view of the fact that responsiveness is allegedly a major virtue of public education.

Note that the parents who object to uniforms or who cannot afford them have no cause for complaint. After all, most schools do not require uniforms. Indeed, the example illustrates one of the public policy advantages of schools for profit over both public and nonprofit schools. Even among the latter, such as Catholic schools, their constituencies are sometimes deeply divided on such matters as the curriculum, dress codes, and extracurricular activities, to mention only a few. In the nonprofit setting, it is often necessary to reach an accommodation on these issues, and the efforts to do so can be as divisive as it is in the public sector. In the for profit sector, however, such differences would constitute a market niche. Instead of being forced to reconcile conflicting views within a single school or system, the entrepreneurial educators would tend to view the differences as an opportunity, not as a problem.

Significantly, existing schools for profit do not necessarily serve the most talented or the most affluent students. On the contrary, the largest group of schools for profit are the schools serving the handicapped or disabled; in fact, there is a national organization of such schools for profit. This is especially interesting because of concerns frequently expressed that public schools would become a "dumping ground" if we strengthen parental ability to choose a private school. The evidence available suggests that a variety of private markets would emerge, or could depend on the specifics of the situation. Significantly, another emerging market is college counselling; proprietary counselling services have emerged as a result of dissatisfaction on the part of high school counsellors as well as parents.

It should also be noted that many parents spend a great deal for educational services to children outside of formal schools. Private music lessons are just one example. We do not have systematic data on the size of the school market for education, but it

undoubtedly runs into tens of billions annually. For example, more and more summer camps offer educational services: mathematics, science, computer education, foreign languages, sports of various kinds -- the specialized educational services offered in summer camps provides additional support for the viability of a market approach. Significantly, one finds very little criticism of out of school instruction for profit; indeed, the subject receives very little attention in the literature on educational policy. One might suppose that if the evils of education for profit were so inevitable, they would have surfaced in the out of school markets for educational services. In this connection, it would be interesting to track the extent to which public school teachers provide educational services on a for profit basis either after school or during vacation periods. I surmise that public school teachers are not opposed to privatization, or to education for profit, as long as the teachers themselves are the ones who reap the profits.

Let me now illustrate the point about incentives by my experience with learning centers for profit. In writing Privatization and Educational Choice, I visited the headquarters of the three major companies: Sylvan Learning Centers, Huntington Learning Systems, and Encyclopedia Britannica. With Sylvan and Huntington, I spent a day going through the program arranged for potential franchisees, that is, persons who are interested in investing $100,000 or more in a learning center.

Let me describe Sylvan's operation briefly. In general, their centers operate from the time schools close to 9:00 p.m., Monday through Thursday. They are also open on Saturdays and during summer and extended vacations.

In the centers, the mode of operation is one teacher for 3 students. Each teacher sits at a table with three students, so there is a high degree of interaction between teacher and students. Fees are set by the franchisees, but we can use $25 an hour as a reasonable average. The teachers are paid $8 to $10 an hour; they may be retired teachers, former teachers seeking part-time work, graduate students, or others deemed qualified. One company uses only certified teachers; the other tries to do so, but accepts qualified exceptions.

The centers have space for a minimum number of tables, perhaps four. Thus if operating at capacity, such a center would have 12 parents paying $25 an hour for instruction, and 4 teachers receiving $32 an hour in toto. If operated six hours a day, the center would gross $1,800 and pay $192 for instruction. The difference ($1,608) must cover rent, utilities, supplies, equipment, advertising, insurance, and salaries and profits for franchisees.

This summary is oversimplified, but accurate enough for present purposes. On the way home from Montgomery, Alabama, where Sylvan's headquarters are located, I was struck by a paradox. During the program for potential franchisees, company representatives frequently referred to differences between their program and the programs of competitors. The latter, however, never included the public schools themselves. On the face of it at least, the public schools could have offered the same program to parents for $10-12 an hour instead of $25. After all, the facilities and equipment were in place. Many overhead costs, such as insurance on the buildings, were already paid for. If public school teachers refused to work for $8 an hour after school, the school district could hire the same teachers who were willing to work at this rate for the learning companies. If union opposition or legal obstacles rendered this impractical, the school system could make the buildings available and provide parents with a list of teachers whom the parents could hire. In other words, the school district could serve as a middleman; the rates charged parents could include a small override to cover school district costs, such as additional custodial or maintenance costs.

In short, there was no obvious reason why school districts could not make these instructional services available for less than half the amounts charged by the learning centers, at no additional cost to the school districts.

The next morning, I called the company officer who had served as my host. I pointed out that in all the discussion about "the competition," no reference was ever made to the possibility that school districts would become part of the competition. In view of the fact that school districts could provide the identical service at less than half the price paid to the learning centers, had the possibility of competition from school districts been considered?

The response was that the companies were not concerned about competition from school districts. We did not discuss the reasons in detail, so I decided to conduct a brief investigation of the issues. At the time, I was teaching graduate courses at the University of Pennsylvania. Most of my students were public school administrators, or teachers who planned to become public school principals or superintendents. When I asked why the public schools did not make the services available, the answers were consistently inadequate. The answer that best explains the situation is one that was never cited by any student. There are no personal managerial incentives to initiate such a change and there are managerial incentives to avoid such action. For example, union opposition was cited, but as someone who has negotiated over 150 school district contracts in six states, I believe union opposition could not block any school board that sincerely wanted to offer the service.

It is always possible to weaken a valid argument by a poor example. Hopefully, I have not done that in this case. To me, the example illustrates some of the inherent advantages of schools for profit over government and/or nonprofit schools. These advantages include:

1. The producers have a direct personal stake in increasing productivity.

2. Education for profit is much more responsive to parental inquiries, needs, and interests. For example, secretaries in the learning centers are trained to record inquiries and how to respond to them. The learning centers must sign up a certain percentage of parents who call for information, hence considerable attention is devoted to telephone procedures.

3. Instructional services can be eliminated, modified, or added much more expeditiously than in public schools.

4. Schools for profit are not subject to the enormous burdens of state regulation and prescription, such as tenure laws, bargaining laws, and employee benefits. Most of this legislation is intended to maximize teacher benefits, even at the cost of student learning.

5. Schools for profit would probably reduce the tremendous litigation costs of public education. These costs arise largely over the need to interpret statutes that are not clear, often deliberately ambiguous. To the extent that education is provided privately, contractual arrangements would tend to resolve problems generated by unclear statutes.

6. Schools for profit would provide a more accurate guide to parent preferences. Markets are clearly superior to political systems on this issue.

Schools for profit would not carry redundant employees on their payroll, whereas public schools are often required to do so by law. In one recent case, the California Supreme Court held that a school district could not refuse to rehire a teacher on the basis of anticipated declines in enrollment; the dismissal could be effectuated only after the enrollments actually declined. Needless to say, inability to act on the basis of anticipated demand would be disastrous to a private sector company.

These are not the only advantages or potential advantages of schools for profit. In fact, I may have omitted the most important: about 50 percent of our high school graduates go on to college; of those who do, about 80 percent enroll in public institutions of higher education. In my opinion, the fact that so many of our young people spend so much of their time in institutions that emphasize redistribution instead of generation of wealth has been harmful. Part-time employment in for profit enterprise does not compensate for this isolation from for profit enterprise. Thus the paradox is that the failure of our educational system to educate is one of the main reasons why the system cannot make the changes that are needed.

What explains the extremely small number of schools for profit? Obviously, the availability of tax supported education underlies the fact that only 10 percent of our schools are private. Still, it does not fully explain why such a small proportion of private schools are for profit. One reason is that most private schools are denominational; religious organizations provide the funding and the supply of students for the majority of private schools.

Inasmuch as religious organizations are overwhelmingly nonprofit, and must be to enjoy tax exemptions and other benefits associated with nonprofit status, the fact that most private schools are not for profit is not surprising. Nevertheless, the proportion of schools for profit would be much higher if state and federal laws did not discriminate against them in various ways. Schools for profit are typically not eligible for benefits provided both public and nonprofit schools. Significantly, public and nonpublic schools have sometimes joined forces to exclude schools for profit from competing on an equal basis; indeed, in the leading case on the issue, a proprietary regional accrediting association composed of public and nonpublic schools refused even to consider a school for profit for accreditation. The refusal was defended despite the fact that accreditation was essential for the proprietary school to participate in various federal programs.

Although schools for profit face some cultural bias, such bias is probably not the major barrier to their expansion. In health care, hospitals for profit have increased dramatically under Medicare and third party payments by health insurers. Similarly, for profit enterprise dominates most independent health services, such as laboratory testing. The increase in health care for profit has cut into the market share of both public and nonprofit providers, and for reasons that would apply to education if and when educational vouchers are enacted.

In my view, failure even to consider the statutory restrictions on education for profit must be viewed as a major weakness in conservative policies on education. This is evident not only with regard to the statutory restrictions on schools for profit but in

the limitations on the authority of school boards to contract for instructional services. The availability of contracted services is heavily influenced by the statutory framework governing the duration of contracts, banking and bidding requirements, bidding procedures, and a host of other matters related to contracted services. Nonetheless, neither the Reagan administration nor the Bush administration to date has evinced any interest in fostering a more hospitable environment for education for profit. A not so benign neglect of the issue characterized the Reagan administration; similarly, the Bush administration has not demonstrated any interest or even cognizance of the issue.

Overall, schools for profit are in a Catch-22 situation. Because they are weak politically, they are not able to block legislation that weakens their ability to compete. Because such legislation continues to be enacted; they are less and less able to compete. The sad truth is that many private school supporters of vouchers and/or tuition tax credits have only a rhetorical interest in competition; their underlying interest is in increased public support, not in increased competition among schools, public or private. Furthermore, of those who seek public assistance for parental choice, most do so to retain an existing constituency, not to expand it as an entrepreneurial enterprise would normally try to do. In short, parental choice must provide schools for profit equal opportunity to compete with public and nonprofit schools. Unless profitmaking schools have a level playing field, parental choice will not generate the benefits associated with competition in the for profit sector.